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No. _____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

ARIZONA FUELS CORPORATION
AND
EUGENE DALTON, PRESIDENT, *Petitioners,*

v.

UNITED STATES OF AMERICA, *Respondents.*

PETITION FOR A WRIT OF CERTIORARI TO THE TEMPORARY EMERGENCY COURT OF APPEALS OF THE UNITED STATES

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QUESTIONS PRESENTED

1. Whether, in an enforcement action brought by the United States seeking to enforce obligations requiring defendants to pay money, a court can impose a statutory civil penalty where the defendants were financially unable to comply with the obligations being enforced?

2. Whether a court can sustain an agency decision as supported by substantial evidence and impose a civil penalty on the basis of facts that were not before nor considered by the agency?

3. Whether, assuming that it can consider evidence outside of the administrative record, a court can base its decision and award of civil penalties on facts that did not exist until after the dates of the violations being enforced?

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v.
UNITED STATES OF AMERICA, *Respondents.*

PETITION FOR A WRIT OF CERTIORARI TO THE TEMPORARY EMERGENCY COURT OF APPEALS OF THE UNITED STATES

The petitioners Arizona Fuels Corporation and Eugene Dalton respectfully request that a writ of certiorari issue to review the judgment and the opinion of the Temporary Emergency Court of Appeals entered in this proceeding on December 24, 1980.

OPINIONS BELOW

The opinions of the Temporary Emergency Court of Appeals and the United States District Court for the District of Arizona, not yet reported, appear in the Appendices hereto.

JURISDICTION

The judgment of the Temporary Emergency Court of Appeals was entered on December 24, 1980. A timely petition for rehearing was denied February 2, 1981, and this petition for certiorari was filed within 30 days of that date. This Court's jurisdiction is invoked under 15 U.S.C.A. §754(a)(1) of the Emergency Petroleum

Allocation Act of 1973 which incorporates by reference §211(g) of the Economic Stabilization Act of 1970, 12 U.S.C.A. §1904n.

STATEMENT OF THE CASE

The petitioner Arizona Fuels Corporation is a small independent refinery operating out of Fredonia, Arizona. It is a family-owned, closely held corporation administered by petitioner Dalton. Up until September, 1980, AFC was certified to run approximately 3000 to 3500 barrels of crude oil per day.

In response to the dramatic increases in the price of crude oil caused by the Arab oil embargo of 1973, the government set up a regulatory program for the control of prices for United States oil. Part of the regulatory reform effort consisted of the entitlements program. That program represented an attempt to equalize the cost to refiners of controlled and uncontrolled oil. Under it, refiners who run a greater percentage of controlled oil than the national average are required to purchase entitlements from those refiners who run a smaller percentage of controlled oil.[1]

Because of the specific congressional intent to preserve the competitive viability of small refiners, several mechanisms were built into the program — like the small refiner bias and the exceptions process — to prevent undue hardships and gross inequity.[2]

Since August, 1975, petitioner AFC has been considered a purchaser of entitlements under the

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[1] 10 C.F.R. §211.67; *Pasco* v. *FEA*, 525 F.2d 1391, (Temp. Em. Ct. App. 1975).

[2] H.R. Rep. No. 531, 93rd Cong., 1st Sess., *reprinted in* [1973] U.S. Code & Admin. News 2582, 2595-2596.

program. At present, AFC's entitlement obligations exceed $30 million.

On September 1, 1977, the government filed a complaint in the U.S. District Court for the District of Arizona alleging that AFC had failed to purchase a substantial amount of its entitlements obligations arising prior to July, 1977, and sought enforcement of those obligations as well as entitlement obligations arising after June, 1977. (R. 11-21).* AFC defended on the grounds that the computation by OHA[3] of its entitlements obligations, as modified through the exceptions process, was erroneous as a matter of law and that, in any event, payment of the obligations would require AFC to operate at a loss and would force it out of business. (R. 32).

On November 28, 1977, the petitioners filed papers arguing that AFC was not financially able to comply with the entitlements orders. (R. 36). Those papers included an affidavit from AFC's president, Dalton, concluding that AFC "is absolutely unable to satisfy the entitlements purchases demanded of it. . . ." (R. 40). On March 6, 1978, petitioners submitted a further affidavit from Dalton concluding that AFC "is and has been throughout this proceeding financially unable to purchase the entitlements. . . ." (R. 48).

[3] "OHA" is the Office of Hearings and Appeals of the Department of Energy. The name of that Office went through changes in the course of the period covered by this litigation. For simplicity's sake, we have referred to that office during the time that it was called the Office of Exceptions and Appeals, and the Office of Administrative Review, consistently as OHA throughout this brief. Similarly, references to the Federal Energy Administration, predecessor in interest of the Department of Energy, and uniformly herein made to "DOE."

* Citations to "(R. _____)" are to the record on appeal before the Temporary Emergency Court of Appeals.

On May 25, 1978, petitioners filed motion papers requesting a hearing on financial impossibility. (R. 59-64). Supporting this motion, an affidavit of Douglas D. Jeppson, an independent, certified public accountant, (R. 65-85), was attached, accompanied by a detailed, seventeen page, certified, audited financial analysis which had been submitted to the Federal Energy Administration and which concluded as of October 31, 1977 (AFC's fiscal year-end) that:

a) With entitlements paid, AFC would have a negative net worth of minus $347,551, (R. 71),

b) If the entitlements obligations were valid, AFC would operate at a net loss (R. 73), and

c) If the entitlements obligations, including those for the following year, were valid "the ability of the Company to continue operation as a going concern would be severely impaired." (R. 80).

On June 8, 1978, petitioners served a notice calling for the hearing on these matters to be set for July 20, 1978. (R. 86-87).

On June 8, 1978, the government moved to limit all evidence at the hearing to the agency's administrative record. (R. 88-89). Petitioners opposed that motion, citing the need for Dalton's testimony as to impossibility of payment. (R. 99-107). On July 10, 1978, the court ruled that it would make its own subsequent determination if any evidence other than the documents considered by OHA was necessary. (R. 4 (7/10/78 minute entry). The district court has yet to make any such determination.

On February 26, 1980, the government submitted its own conclusion as to the petitioners' ability to pay,

informing the district court that "the magnitude of their entitlements obligations now exceeds the value of their corporation." (R. 174)

The district court ordered that a hearing be held on April 3, 1980, on what would, in effect, be the issue of AFC's inability to pay its entitlements obligations. (R. 189-190). On March 28, 1980, defense counsel notified the district court that AFC intended to submit financial data at that hearing to demonstrate that AFC's revenues, after deductions for AFC's expenses, would not leave enough to pay the entitlements, and further would cover evidence on what the district court described as "how" much money is now in the possession of the company and of the individual. . . ." (R. 220). On March 31, 1980, however, the district court observed *sua sponte* that counsel for the government had not had adequate opportunity to review discovery materials and ordered that the April 3, 1980 hearing be vacated. (R. 300, 308, 312).

On May 3, 1980, petitioners took the deposition of James J. Fenton, Program Manager of the Small Refiner Branch of DOE and the government's principal auditor for this litigation. With respect to all the years at issue here, Mr. Fenton deposed that payment of the entitlements ordered by OHA would have required AFC to operate at a loss in each year (1975, 1976, 1977, 1978, 1979, and 1980 to date), (R. 559-561), and that with respect to the most substantial period of entitlement obligations (November 1, 1977 to at least October 31, 1979 — no opinion having been reached as to 1980) AFC simply did not have the financial resources to make entitlements payments. (R. 557-558).

On May 6, 1980, a hearing was held in Phoenix. Dalton and Quinn Stirland, AFC's chief financial

officer, came down from Salt Lake City for the purpose of providing testimony and other evidence on what defense counsel described to the court as "the question of Arizona Fuels' contentions that it is financially incapable of purchasing entitlements. . . ." (R. 332). Counsel for the government objected to the conduct of the evidentiary hearing prior to argument on a government discovery sanction motion. (R. 333). The court ordered petitioners to address the discovery issues before presenting evidence on the impossibility issue. (R. 334).

On May 7, 1980, at the conclusion of the hearing on the discovery issue, the court determined that it would not at that time impose any of the sanctions requested by the government. (R. 537). With respect to the petitioners' continuing request for an evidentiary hearing on the net loss and impossibility issues, the court ruled from the bench that "(a) hearing on the defendants' claim of financial inability to pay the monthly entitlements will be held upon the application of the attorneys for the Government . . ." after discovery is completed. (R. 537-538). The court also ruled that "incidentally, at that hearing we will also entertain and decide the other motions that are pending before the court, the motions for summary judgment and so forth." (R. 541).

Petitioners also had submitted for consideration copies of the audited financial statement of Arizona Fuels for the 1978 fiscal year. (R. 670-689). That statement showed that petitioners did not have the cash available to purchase the entitlement obligations as they accrued.

AFC's 1978 fiscal year statement presented a picture of a financially troubled firm. (R. 670-689). In that year,

AFC's entitlements liability exceeded $13 million (R. 674) but it had cash and unencumbered TCDs of only $1,424,618. (R. 673, 680, 685). Not only did AFC again show a negative working capital and negative stockholders equity, but also it sustained a negative *gross* profit of $481,819. (R. 676), which means it could not have operated at a profit even if it had not paid its overhead expenses, such as salaries and wages. Again, the auditors issued a "going concern" qualification with their statement. (R. 672).

In addition, the 1979 balance sheet showed that AFC had total assets of only about $14 million (R. 745) compared to obligations exceeding $24 million. (R. 325).

No hearings were held in the period from May 7, 1980, the date of the hearing referred to immediately above, through June 26, 1980. On June 26, 1980, the district court entered the judgment here appealed, (Appendix C at 9a), requiring petitioners to pay all entitlements at issue and imposing a civil penalty on both petitioners in the amount of $1,000,000.

The district court characterized all of the monthly entitlements obligations as falling into one of two exclusive classes: final orders, *i.e.* , those pre-July, 1977 OHA orders which were not eligible for review by the Federal Energy Regulatory Commission, and "non-final decisions," *i.e.*, those post-June, 1977 orders which were eligible for review by the Federal Energy Regulatory Commission and all of which, in fact, had been submitted to that Commission by AFC for administrative review. Appendix C at 9a; *See also* Appendix A at 4a.[4]

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[4] FERC has not yet reached any determinations on the merits of any of those appeals, which are docketed with the Commission as Nos. RA79-4, RA79-22, and RA80-44.

The district court's finding as to the final orders was confined to a finding that OHA's decisions were supported by substantial evidence. Appendix A at 4a. The district court expressed no explicit conclusions as to issues of law.

With respect to the final orders, the district court entered judgment for payment in full of $941,432.00, plus prejudgment interest of $325,459.74. (R. 584).[5]

The district court found that "[t]he record is replete with evidence of defendants' willful failure to pay its entitlement obligations" (Appendix B at 7a), and imposed a civil penalty of $1,000,000.00 on AFC and Dalton. Appendix C at 9a. AFC objected, asserting that there was no such evidence in the record. (R. 552-553). The district court then amplified its findings, citing three series of transactions aggregating approximately $3,000,000 at any time (Appendix D at 12a), and questioning certain AFC accounts held in nominee form (*Id.*), all of which were, however, properly reported as AFC accounts (R. 418-419). The district court found that AFC had offered no evidence that the transactions were ordinary and necessary expenses. (Appendix D at 12a).

On December 24, 1980, the Temporary Emergency Court of Appeals issued a decision affirming in part and reversing in part the district court's June 26, 1980 judgment. *United States* v. *Arizona Fuels Corporation*, Nos. 9-53, 9-54 (Temp. Em. Ct. App., Dec 24, 1980)

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[5] With respect to the non-final, or post-June, 1977, transactions, the court ruled that all claims of the government on the merits of these orders would be dismissed, but ordered that AFC and Dalton make full and immediate payment on all the non-final orders. These obligations, through February, 1980, total $24,120,198. (R. 325).

(Appendix E at 15a). Petitioners had appealed to the Temporary Court of Appeals from those portions of the district court's judgment imposing civil penalties on defendants, ordering defendants to pay the pre-July, 1977 entitlements obligations and ordering defendants to comply with the entitlements program. *Id.*, No. 9-53.[6] The court of appeals affirmed the district court stating that petitioners had not met their burden of showing impossibility, and finding that petitioners did have the resources to purchase their pre-July, 1977 obligations. Appendix E at 20a-23a.

REASONS FOR GRANTING THE WRIT

I. The Decision Below Presents An Important Question On The Scope Of Permissable Use Of Civil Penalties In Cases Brought To Enforce Compliance With Administrative Regulations.

An increasing number of statutes establishing regulatory programs provide for the imposition of civil penalties against regulated individuals held to be in violation of the pertinent laws and administrative regulations. *See generally,* Lawrence, *Judicial Review of Variable Civil Money Penalties,* 46 U. CINN. L. REV. 373 (1977); Diver, *The Assessment and Mitigation of Civil Money Penalties by Federal Administrative Agencies,* 79 COL. L. REV. 1435 (1979). In fact, as of 1979, there existed 348 statutory civil penalties that could be imposed by federal agencies. *Diver, supra* at 1438.

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[6] The government had appealed from that portion of the district court's opinion that had dismissed as nonfinal the obligations arising after July, 1977. *United States* v. *Arizona Fuels Corporation*, No. 9-54 (Temp. Em. Ct. App., Dec. 24, 1980). The court of appeals reversed that portion of the opinion and remanded it for reconsideration by the lower court.

Because the civil penalty sanction has proved to be a simpler, more effective technique of enforcement, it "has assumed a place of paramount importance in the compliance arsenal of federal regulations." *Id.* at 1436. In 1977 alone, $52,000,000 was collected by the federal government through the imposition of civil fines. *Id.* at 1445.

In most situations, the agency must invoke the jurisdiction of the district court in order to collect civil fines. *Id.* at 1439. As this Court stated as early as 1893 "[f]rom the earliest history of the government the jurisdiction over actions to recover penalties and forfeitures has been placed in the District Court." *Lees* v. *United States,* 150 U.S. 476, 478 (1893). It is generally accepted that the defendant in an enforcement proceeding may present the court with evidence to mitigate the penalty. *See, e.g., United States* v. *Swingline, Inc.,* 371 F. Supp. 37 (E.D.N.Y. 1974); *United States* v. *Bradley,* 252 F. Supp. 804 (S.D. Tex. 1966). Some statutes detail the considerations which should be considered in determining the amount and mitigation of the civil penalty. *See. e.g.* The Coal Mines Health and Safety Act, 30 U.S.C. §820(i) (Supp. 1980). Yet, in most situations, detailed factors for mitigation are not provided (*Diver, supra* at 1443), and thus, it is left to the district courts to determine what facts are relevant to a defense against imposition of a fine. *See, e.g., United States* v. *ITT Continental Baking Co.,* 420 U.S. 223, 229n.6 (1975); *Porter* v. *Warner Holding Co.,* 328 U.S. 395 (1945).

The case law on awards of civil penalties does not evidence a uniform approach to the defenses available to civil penalty sanctions. *See generally,* Lawrence, *Judicial Review of Variable Civil Money Penalties,* 46 U. CINN.

L. Rev. 373 (1977). Thus, civil penalties have been denied or mitigated in various cases because the violation was not flagrant (*United States* v. *Garrett,* 296 F. Supp. 1302 (N.D.Ga. 1968) *aff'd,* 418 F.2d 1250 (5th Cir. 1969) *cert. denied,* 399 U.S. 927 (1970)), because a penalty would serve no purpose (*Wentz Heating & Air Conditioning Co.* v. *Federal Energy Administration,* 410 F. Supp. 1155 (D. Neb. 1976)), because the violation did not result in any actual injury (*United States* v. *Newman,* 331 F. Supp. 1240 (D. Hawaii 1971), and because the lawsuit had been friendly. *United States* v. *Bradley,* 252 F. Supp. 804 (S.D. Tex. 1966). In other cases, the courts have balanced several factors such as the public interest, the inability of the defendant to comply, and the defendant's good or bad faith. *United States* v. *J.B. William Company, Inc.* 354 F. Supp. 521, 548 (S.D.N.Y. 1973) *rev'd in part on other grounds*, 498 F.2d 414 (2d Cir 1974). *See also United States* v. *Ancorp National Services, Inc.,* 367 F. Supp. 1221 (S.D.N.Y. 1973) *aff'd,* 516 F.2d 198 (2d Cir. 1974).

Although the actual assessment of an award of civil penalties has been held to a be a matter of judicial discretion (*United States* v. *ITT Continental Baking Co.,* 420 U.S. 223, 229n.6 (1975)), the above cases indicate that guidance is needed as to what factors are relevant to an exercise of that discretion and what defenses are available to the defendant. The importance of this issue is underscored by the increased use of the civil penalty by agencies in enforcement proceedings.

The instant case presents the narrow question of whether impossibility of compliance can constitute an affirmative defense to the imposition of an award of civil penalties. Yet, although the case involves the assertion of only one defense, the uniqueness of that defense in relation to the facts presented by the instant case will enable the Court to use this case as a vehicle

for development of the policy justifications and guidelines for the lower courts to use as a basis for determining what factors are relevant to mitigation or denial of an award of civil penalties.

In other areas involving the exercise of discretion, this Court has held that the inquiry should focus on the purposes to be served by the sanction or remedy in question. *See e.g., Shillitani* v. *United States,* 384 U.S. 364 (1966); *Maggio* v. *Zeitz,* 333 U.S. 58 (1947); *Jacob Siegal Co.* v. *Federal Trade Commission,* 327 U.S. 608 (1946). *See also generally,* Lawrence, *Judicial Review of Variable Civil Money Penalties,* 46 U. CINN. L. REV. 373 (1977). The cases in which such an inquiry has been made have often dealt with the claim of impossibility of compliance. *See, Shillitani, supra; Maggio, supra; United States* v. *Park,* 421 U.S. 658 (1975). Thus, for example, in *United States* v. *Park,* the Court recognized the availability of the defense of objective impossibility in the case of the alleged violation of an act providing for criminal fines and imposing "the highest standard of care" upon the regulated parties.

The purpose underlying an award of civil penalties is to inspire compliance and to deter or prevent future violations of the law and regulations in question. *United States* v. *ITT Continental Baking Co.,* 420 U.S. 223, 229n.6 (1975); *United States* v. *Hess,* 317 U.S. 537, 549 (1942). Thus, civil penalties are remedial and coercive in nature rather than punitive. Because of these justifications, civil fines are analogous in effect to civil contempt sanctions.[7]

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[7] *See, United States* v. *Swingline,* 371 F. Supp. 37 (E.D.N.Y. 1974); *United States* v. *J.B. Williams Company, Inc.,* 354 F. Supp. 521, 530 (S.D.N.Y. 1973) *rev'd in part on other grounds,* 498 F.2d 414 (2d Cir. 1974).

In cases involving civil contempt, it is traditionally and uniformly held that inability to comply constitutes a complete defense. *Shillitani* v. *United States,* 384 U.S. 364, 368, 371 (1966); *Maggio* v. *Zeitz,* 333 U.S. 58, 72 (1977). The rationale behind permitting such a defense is that if the contemnor lacks the ability to comply with a court order, neither the coercive or deterrence purposes will be served by imposition of the sanction. *Shillitani, supra* at 371. Rather, to hold a party in civil contempt, despite his inability to comply, would be to use the contempt power as a mechanism of punishment. *Maggio, supra,* at 72.

In the instant case, the civil penalty statute does not provide factors for the court to consider in mitigation of a penalty. 15 U.S.C. §754(a)(3)(A). The district court, after finding that defendants had violated DOE regulations, imposed a $1 million civil penalty. Although the district court did not detail the factors it considered in making this award, it stated that "[t]he record is replete with evidence of [defendants'] willfull failure to pay entitlement obligations." Appendix B at 7a. In that order, the court did not refer to or apparently consider the defendants' contentions that they were financially unable to comply — a contention that, as the Statement of the Case indicates, was repeatedly brought to the attention of the court — despite the fact that the court had before it petitioners audited financial statements which clearly indicated their incapacity to comply.[8]

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[8] In a later order by the court, issued upon petitioners motion to stay the June 26 order, the court referred to petitioners' assertion that they were financially unable to comply. Appendix D at 12a. The court stated that petitioners had failed to show inability. *Id.* Yet, this assertion is belied by the fact that the court had before it all of petitioners financial statements and other evidence in the form of affidavits. In other cases, the district courts have not

The award of civil penalties in the instant case will not serve a coercive or deterrent function, or the purposes underlying the Emergency Petroleum Allocation Act of 1973.[9] The imposition of the award, in fact, makes it more difficult, if not impossible, for the defendants to comply with their outstanding obligations — those initially held to be non-final by the district court. At the time of the district court decision, petitioners' entitlements exceeded $24 million. (R. 325). Yet their total assets were only $14 million. (R. 746). Thus, imposition of the fine in the instant case is punitive in nature.

Because of the increasing importance of the civil penalty in enforcement actions, the need for definitive guidelines, and the peculiarly inequitable result in the instant case, this Court should grant this petition for review.

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required more than such evidence from petitioners seeking to mitigate a civil penalty on the basis of financial inability. *See, e.g., United States* v. *J.B. Williams Company, Inc.,* 354 F. Supp. 521, 548 (S.D.N.Y. 1973) *rev'd in part on other grounds*, 498 F.2d 414 (2d Cir. 1974).

[9] 15 U.S.C.A. §751 *et. seq.* (1976) At least one author has asserted that if the court is going to consider the purposes behind the legislation allegedly violated in making an award of civil penalties, the court should look at the entire framework and objectives of the enactment, rather than focusing on a single objective. Lawrence, *Judicial Review of Variable Civil Money Penalties,* 46 U. CINN. L. REV. 373, 407 (1977). In this regard it should be noted that it was Congress' express intent that the regulations adopted to enforce the Emergency Petroleum Allocation Act should be administered in a manner so as not to destroy the competitive viability of small, independent refiners. H.R. REP. NO. 531, 93d Cong., 1st Sess., *reprinted in,* [1973] U.S. CODE CONG. & ADMIN. NEWS 2582, 2595-2596.

II. The Courts Erred By Relying On Evidence Outside The Administrative Record In Order To Hold That The Agency's Decisions Were Supported By Substantial Evidence.

A second factor in the instant case which supports the Court's granting petitioners' request for a writ of certiorari is the fact that the courts below exceeded the scope of judicial review by relying on evidence outside the administrative record in order to find the agency's decisions supported by substantial evidence.

As indicated in the Statement of the Case, the instant case involved a single suit by the government in which it sought enforcement of the agency's entitlement obligation orders. Thus, in effect, the case involved several different orders and different agency determinations. The district court held that the pre-July, 1977 obligations were final orders and granted summary judgment for the government on the issue of whether the agency's denials of exception relief as to those obligations was supported by substantial evidence.

Under the administrative procedures, the agency issues a monthly notice of each refiner's entitlement obligation. 10 C.F.R. §211.67; *Pasco, Inc.* v. *Federal Energy Administration,* 525 F.2d 1391 (Temp. Em. Ct. App. 1975). The agency's computation is based upon information submitted by each refiner concerning its crude oil runs to stills and other information about the business. *Id.* An opportunity was afforded by Congress and the agency for refiners to apply for exceptions relief if payment of their obligations would cause substantial hardship or gross inequity. 10 C.F.R. §205.50. In order to apply for such relief, refiners must submit financial projections for the period in which the entitlements obligation will impact refinery operations. *Id.* OHA's

grant or denial of exceptions relief is confined to findings of fact based upon the above information.

Under the substantial evidence standard of review, a court reviews the record as it existed at the time of the agency decision in order to determine if a reasonable factual base exists for the agency action. *Federal Power Commission* v. *Transcontinental Gas Pipeline Corp.*, 432 U.S. 326 (1976); *N.L.R.B.* v. *Jones & Laughlin Steel Corp.*, 331 U.S. 416, 422 (1946). ("... unless the order was valid when it was issued, there is no basis whatever for it and no court can decree its enforcement in the future"). In other words, material relating to events subsequent to the agency decision are not considered by a court because they were not in the agency's record, and thus, played no part in the agency's decision.

> ... [the substantial evidence] standard goes to the reasonableness of what the agency did on the basis of the evidence before it, for a decision may be supported by substantial evidence even though it could be refuted by other evidence that was not presented to the decision-making body.

United States v. *Carlo Bianchi & Co.* 373 U.S. 709, 715 (1963). The converse of the above is equally true in that a court cannot sustain an agency decision on the basis of evidence outside of the administrative record or on grounds not relied upon by the agency. A court may not "supply an alternative, unstated ground to support an agency's decision if that ground is one that 'the agency alone is authorized to make.' " *Gulf States Utilities Co.* v. *Federal Power Commission,* 411 U.S. 747, 764 (1973).

The above propositions are equally true in relation to cases arising under the Emergency Petroleum Allocation Act of 1973. Section 5(a)(1) of the Act provides that judicial review of the agency's orders will

be confined to a determination on whether its action is in excess of agency authority, or based upon findings that are not supported by substantial evidence. 15 U.S.C. §754. *See also, Basin, Inc.* v. *Federal Energy Administration,* 534 F.2d 324 (Temp. Em. Ct. App. 1976) *cert. denied,* 434 U.S. 821 (1977); *Chrysler* v. *Dunlop,* 490 F.2d 985, 988 (Temp. Em. Ct. App. 1973); *Pacific Coast Meat Jobbers Ass'n* v. *Cost of Living Council,* 481 F.2d 1188 (Temp. Em. Ct. App. 1973); *Wentz Heating & Air Conditioning Co.,* 410 F. Supp. 1155, 1157 (D. Neb. 1976) (review of enforcement proceeding). Therefore, in the instant case, the courts could legitimately review only those facts that existed at the times in 1977 and before that the defendants applied for exception relief.

In affirming the district court decision, the Temporary Emergency Court of Appeals found that ". . . the company could easily have paid these (pre-July, 1977) obligations." Appendix E at 22a. In support the court of appeals stated:

> The cause of Arizona Fuels' financial condition is not the entitlements program, from which defendants profited, but is defendant Dalton's draining away from Arizona Fuels of its financial resources.

Id. Earlier, in its opinion, the court of appeals made a specific reference to the actions of petitioner Dalton which it felt necessitated affirmance of the agency's actions.

> . . . [T]he record indicates that they [petitioners] could easily have complied at least with the "final" entitlement obligations due for the period August 1975 to July 1977. The sum of over $2.5 million which Arizona Fuels lent to Dalton and which Dalton used to purchase a cattle ranch for himself would easily have covered Arizona Fuels' entitlement obligations for this period.

Id. at 21a. Yet, the transaction referred to by the court of appeals did not occur until long after July, 1977. (R. 757-758). In fact, the funds and expenditures recited in the government's reply brief to the court of appeals related to time periods subsequent to July, 1977. Brief of Appellee at 2-7, *United States* v. *Arizona Fuels Corp*; No. 9-53, (Temp. Em. Ct. App. Dec. 24, 1980).

Even assuming the validity of the court's rationale, the loan to defendant Dalton and the transactions relied on by the government on appeal could not have formed the basis for OHA's denial of exceptions relief for defendants' pre-July, 1977 entitlement obligations. The court of appeal's reliance on the loan, therefore, was beyond the permissible scope of judicial review of agency actions in that it relied on evidence outside of the administrative record, (*Federal Power Commission* v. *Transcontinental Gas Pipeline Corp.*, 423 U.S. 326 (1976)), and justified actions on grounds not relied upon by the agency. *Gulf States Utilities Co.* v. *Federal Power Commission,* 411 U.S. 747 (1973).

The court of appeals' decision is in direct disregard of and in conflict with the decisions of this Court, thus necessitating a review and remand.

III. The Decision Below Presents An Important Question In The Area Of Enforcement Of The Actions Of Administrative Agencies With Regards To What, In Terms Of Administrative Law And Relevancy, May Constitute An Appropriate Evidentiary Basis For An Award Of Civil Penalties.

In its decision, the Temporary Emergency Court of Appeals upheld the district court's imposition of a $1 million penalty for petitioners' failure to purchase their pre-July, 1977 entitlement obligations. Appendix E at

20a-21a, 23a. The court of appeals affirmed the district court's finding of willfulness and further stated that petitioners had the financial resources to "easily" comply with "at least with the 'final' entitlement obligations due for the period August 1975 to July 1977." *Id.* at 21a. In support of its latter finding, the court referred to the sum which Arizona Fuels had loaned to petitioner Dalton. *Id.*

As was discussed in the previous section, the transaction relied upon by the court of appeals occurred long after the pre-July, 1977 entitlement obligations became final. The questions arise as to whether it is appropriate for a court to base a civil penalty award on evidence concerning a party which is remote in time from the violation that constitutes the justification for the award, and, if use of such evidence is permissible, can a court justify imposition of a fine on the basis of an isolated transaction without reviewing all of the party's actions and financial resources from the time of the violation to the time of suit, including the party's present ability to comply.

With regards to the first question, it should be noted at the outset that, in the instant case, the court of appeals held that entitlement obligations are "payable at the end of each month in which they were published by the Department in the Federal Register." Appendix E at 20a. If this requirement is not met, therefore, the refiner is in violation of the agency's regulations. The refiner, under the regulations, may appeal or seek adjustment of the published obligation, but such a recourse under the court of appeals' decision apparently would not absolve or negate the violation if the refiner does not purchase its obligations within the regulatory period. In fact, the agency's traditional practice had been to provide the adjustments granted through the exceptions or appeals

process prospectively. *See e.g., Continental Oil Co.*, 2 FEA ¶ 83,344 (Oct. 14, 1975). Although the agency's exceptions and appeals process may eventually produce an equitable adjustment for the particular refiner, under the court of appeals decision a refiner would still be in violation of agency regulations if it failed to purchase its entitlements within the regulatory period even if it did not have the financial resources in the particular month to absorb the expense. Therefore, it would appear that inability to comply, though relevant to an adjustment in the future, would not be considered a defense to the initial violation of the refiner's failure to purchase its entitlements obligation upon publication by the agency.

The refiner's failure to purchase its entitlements within the month of publication constitutes the violation upon which an award of civil penalties is based. Although a refiner's inability to comply on the date the obligation is due would not excuse the violation, it is pertinent to the necessity for a civil penalty sanction.

As discussed more fully above, the justifications for an award of civil penalties are to coerce compliance and to deter future violations. *See* discussion, *supra* pp 12-13. The necessity for a fine has been held to be a matter of judicial discretion, (*United States* v. *ITT Continental Baking Co.*, 420 U.S. 223, 229n.6 (1975)), and necessarily is equitable in nature. To base an award of civil penalties on evidence of the party's conduct or condition months or years subsequent to the time of the violation, as was done in the instant case, ignores the crucial questions as to why the violation occurred, will it serve the purpose of coercing future compliance, and will it deter similar violations.

If a refiner is financially unable to purchase its obligations when due, the fact that it subsequently may

obtain the ability, cannot be said to negate the fact that at the time of the violation, the refiner did not have the resources to comply. Thus, to justify an award of civil penalties on the grounds of a later acquisition of resources will not serve to coerce or deter future similar violations. Under the regulatory format, if in the future, a refiner again lacks the financial ability to purchase its entitlements when due, it will risk a violation despite the past impositions of civil fines.

Therefore, in the instant case, the court of appeals' use of evidence relating to a transaction which occurred long after the administrative violations in issue was to base the civil penalty award on factors irrelevant and remote to the scope of the violations and the justifications for imposition of such a fine. Business relationships and financial health, especially today, are constantly in flux. The defendants' financial posture prior to July, 1977 differs from that presented in subsequent years. The fact that petitioners allegedly had funds available in 1978 or 1979 does not mean or make it more probable that those funds were available and, therefore, the petitioners were financially able to comply when the pre-July, 1977 entitlement obligations became due. Each financial period presents a different financial picture containing different costs, expenditures, operations, business judgments and entitlement obligations. In effect, what the court of appeals did in the instant case was to use a source of funds allegedly available in a later period in order to establish the fact of petitioners' financial ability to comply in a prior period.

In analogous situations, the courts have held that evidence of like subsequent situations were irrelevant and remote to the prior conduct which formed the basis of

the suit. The issue is characterized as a matter of relevance. One factor in determining the relevance of evidence to a particular issue is the remoteness of the event or information to the circumstances involved in the particular issue being litigated. *See, e.g., International Shoe Machinery Corp.* v. *United States Shoe Machinery Corp.*, 315 F.2d 449 (1st Cir.) *cert. denied*, 375 U.S. 820 (1963). Thus, for example, the costs incurred by a second contractor in completing a construction could not be used to project the costs of the first contractor because of changed conditions and circumstances. *See, Paul Hardeman, Inc.* v. *Arkansas Power & Light Co.*, 38 F. Supp. 298, 315-316 (E.C.Ark. 1974). And, it has been held that in assessing punitive damages, evidence of the defendant's conduct subsequent to the time of injury is irrelevant. *Thomas* v. *American Cystoscope Makers, Inc.*, 414 F. Supp. 255, 265 (E.D.Pa. 1976).

In addition, the action of the Temporary Emergency Court of Appeals is analogous to those cases that have arisen under Fed. R. Evid. 404(b). It is generally held under that rule that evidence of subsequent events unrelated to the act in issue cannot be used in order to prove the existence of that act. *See, e.g., United States* v. *Boyd*, 595 F.2d 120 (3rd Cir. 1978); *United States* v. *Bledsoe*, 531 F.2d 888 (8th Cir. 1976); *United States* v. *James*, 555 F.2d 992 (D.C. Cir. 1977); *United States* v. *Manafzadeh*, 592 F.2d 81 (2d Cir. 1979).

There appears to be no rational reason to treat the permissible evidence in an enforcement action seeking civil penalties in a different manner, especially in a situation where use of such evidence would not be consistent with the purposes and policies underlying an award of civil fines.

To find that the expenditures and allegedly available funds in 1978 and 1979 prove petitioners' ability to have complied in 1977 is prejudicial to petitioners'. Certainly, if those funds were available to petitioners, they could have covered the pre-July, 1977 obligations. Yet, at the time of the loan to petitioner Dalton was made, petitioners had accrued entitlement obligations amounting to several million dollars over that loaned to petitioner Dalton and, in fact, more than the actual worth of the corporation if liquidated. Therefore, the court of appeals based its decision on a sum of money that not only did not exist during the pertinent time but also would not have satisfied even one-half of the obligation imposed by the agency at the time the expenditure was made.

Assuming that the court did not err in basing its decision on the loan to petitioner Dalton, the question arises as to whether a court can justify imposition of a civil fine on the basis of an isolated transaction without reviewing all of the party's actions and financial resources from the time of violation to the time of suit, including the party's present ability to comply.

As mentioned previously, actions seeking civil penalties are analogous to proceedings for civil contempt. *See* discusion, *supra*, pp. 12-13. With regards to civil contempt proceedings, this Court has held that the courts must examine all of the evidence of events occurring subsequent to the violated order, and place particular emphasis on the contemnor's *present* ability to comply. *Maggio* v. *Zeitz*, 333 U.S. 59, 76 (1947). Thus, even if prior events showed that a party could have complied, if at the time of the contempt charge he had lost that ability, a judgment of civil contempt should not be issued. *Id.* at 75-77. The rationale underlying this

proposition rests upon the fact that to hold one in civil contempt who lacks the present ability to comply would be to inflict punishment upon the alleged contemnor, and, therefore, be contrary to the policies underlying the civil remedy. *Id.* at 72.

In the instant case, the court of appeals justified the award of civil penalties on the basis of isolated transactions which occurred more than a year after the violation in question. There is no indication in the court's opinion that a review of all of petitioners financial affairs and resources from the time of the violation to the time of the district court judgment was conducted. In fact, if such a review had been conducted, it would have shown that at the time of judgment, the petitioners entitlement obligations exceeded $24 million dollars (R. 325) whereas their total assets were only $14 million. (R. 746) At the end of 1979, the petitioners had little in cash and unencumbered TCD's and showed a negative stockholders equity (R at 746). Instead of weighing these facts, the court merely recited the loan to Dalton as justification for the civil fine. Such a result is prejudicial to petitioners, and uses the civil penalty as a mechanism of punishment.[10]

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[10] The court of appeals also stated that petitioners had not met their burden to show financial inability, and that their assertion that a hearing should have been held "ill suits them in light of their consistent failure to present substantial evidence of impossibility of compliance, despite numerous opportunities." Appendix B at 21a. Yet, as is indicated in the Statement of the Case, petitioners had repeatedly expressed their desire and preparedness to have an evidentiary hearing but their opportunity to do so was repeatedly delayed due to motions by the government and *sue sponte* rulings of the district court. In addition, all of petitioners' financial statements and some affidavits concerning their financial condition, as is briefly depicted above, were contained in the record of the district court.

The above discussion indicates both the evidentiary problems confronted in an enforcement proceeding seeking civil penalties, and the appropriateness of the instant case as a vehicle for this Court's review of the question.

CONCLUSION

For the above stated reasons, a writ of certiorari should issue to review the judgment and opinion of the Temporary Emergency Court of Appeals.

Respectfully submitted

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APPENDIX

APPENDIX A

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

No. CIV 77-689 PHX CAM

UNITED STATES OF AMERICA, *Plaintiff,*

v.

ARIZONA FUELS CORPORATION, and EUGENE DALTON, President, *Defendants.*

Order

(Filed March 25, 1980)

The above entitled and numbered cause of action was filed on September 1, 1977.

Upon application and hearing held September 26, 1977, this Court entered an Order, filed September 27, 1977, ordering Defendants Arizona Fuels and Eugene Dalton to comply with the Old Oil Entitlements Program as set forth in 10 C.F.R. §211.67 and, in essence, not to waste the assets of the corporation.

Upon application and hearing held November 29, 1977, the Temporary Restraining Order filed September 27, 1977, was continued in effect.

On February 9, 1978, an Order to Show Cause was entered, requiring Defendants to appear and show cause why they should not be held in contempt for failure to comply with the Court's Orders of September 27, 1977, and November 29, 1977. After complete briefing by the parties, a hearing was held on the matter. At the hearing, held March 6, 1978, the Court heard the arguments of the parties and was available to hear any arguments or evidence presented by Defendants. By Order of April 13, 1978, the Court ruled that Defendants had not shown good cause why they should not be required to comply with the prior Orders of the Court. The Court also held that it was Defendants' burden to show that they could not comply with the Court's Orders and stated that

any such showing "should include the production of defendants' books at any future hearings on this matter to substantiate the claim, and the appearance of defendant to take the stand and testify under oath, as well as any other testimony or other evidence that defendant deems appropriate."

On July 20, 1978, the Court heard oral argument on Defendants' Motion for Reconsideration and Motion for Stay, both filed May 25, 1978, in which Defendants sought reconsideration and stay of the Court's April, 1978, Order. After consideration of the evidence, arguments and authorities presented, the Court ordered, by way of written Order entered July 20, 1978, that: Defendants establish an escrow account within 5 days of entry of the written Order and to provide the Court with documentary proof of the account; purchase, through the Department of Energy (DOE), entitlements in the amount of $444,290.98, within 10 days of entry of the Order, said amount being the sum of all funds received from an interpleader proceeding in the United States District Court for the District of Utah; and, *inter alia,* comply with the entitlements purchase requirements of 10 C.F.R. §211.67. The Court also provided that "[s]hould defendants fail to comply with this Order, a Bench Warrant shall issue forthwith for the President of Arizona Fuels Corporation, Eugene Dalton."

To date, the only sums paid by Arizona Fuels toward the purchase of entitlements, since institution of this lawsuit, are the funds noted above, Defendants have made no appropriate effort, in accordance with the Court's Orders, to convince the Court that they are unable to comply with the Court's Orders. There has been no evidence presented from which the Court could find that a good faith effort to comply with the Court's Orders has been made by Defendants. At no time have the Defendants sought a stay from DOE as provided by 10 C.F.R. §205.120, *et seq.*

At the July 20, 1978, hearing, the Court entered an Order from the bench requiring the parties to submit cross-motions for summary judgment. In response to that Order,

Defendants submitted "Defendants' Memorandum Submitted Pursuant to This Court's Order of July 20, 1978", said Memorandum being filed September 1, 1978. In essense, the memorandum stated that the presence of genuine issues of material fact precluded Defendants from filing a motion for summary judgment and that discovery needed to be had before such a motion could be filed. Plaintiff filed its cross-motion for summary judgment on September 11, 1978. In response to Plaintiff's cross-motion for summary judgment, Defendants filed, on September 21, 1978, a motion to dismiss certain of Plaintiff's claims or, in the alternative, for a stay, and a memorandum in opposition to Plaintiff's motion for summary judgment.

Oral argument on the motions was heard on October 30, 1978, and the matters were taken under advisement. The parties submitted supplemental information and briefs with the last submission being filed on March 5, 1979. In June 1979, this matter was inadvertently transferred to the Honorable Valdemar A. Cordova upon his installation as United States District Judge for the District of Arizona. On February 11, 1980, the matter was transferred back to this Court for resolution of matters that had been previously argued.

On the 29th of February, 1980, upon application of Plaintiff, the Court entered an Order to Show Cause, directing Defendants to appear and show cause why they should not be held in contempt for failure to comply with the Court's Orders of September 27, 1977; November 29, 1977; April 13, 1978; and July 20, 1978. Memoranda were filed, including Defendants' motion to dismiss non-final administrative actions. The matter was duly heard on March 17, 1980.

The Court's Order of April 13, 1978, set forth the showing that Defendants need undertake to show why they should not be held in contempt for failure to comply with the Court's prior Orders. Defendants have made no attempt to produce competent evidence of their inability to comply with

the Old Oil Entitlements Program. Instead, Defendants argue that they have complied with the Court's Orders by seeking exception relief, as provided by 10 C.F.R. §205.50, *et seq.* This argument, considered in light of Defendants' failure to seek a stay of application of the Secretary's orders in accordance with 10 C.F.R. §205.120, *et seq.*, carries no weight.

Defendants have failed to bring forth any evidence that could be construed to show that a reasonable effort has been made to comply with the entitlements program.

Furthermore, the Court, having reviewed and considered the pleadings, regarding Plaintiff's cross-motion for summary judgment filed September 11, 1978, and the related pleadings filed by both parties, including Defendants' motion to dismiss or for stay, the transcript of hearing held with respect to said motions, the administrative record submitted with said motions, and the authorities cited by the parties, finds that the record reflects that the appeals decisions upholding the Department's denial of exception relief to Defendants are supported by substantial evidence.

In light of the foregoing,

IT IS ORDERED that Plaintiff's Cross-Motion for Summary Judgment, filed September 11, 1978, is granted with respect to all entitlements obligations incurred prior to July, 1977, for the reasons that the decisions are supported by substantial evidence and for failure to comply with Orders of this Court. Rules 55(b)(2) & 56, Fed. R. Civ. P.

The Complaint is dismissed with respect to all non-final decisions of the Department of Energy from which appeals have been taken;

The Court's prior Orders remain in effect with respect to Defendants' obligation to purchase entitlements, and dismissal of the Complaint with respect to non-final agency actions shall not prevent the Plaintiff from seeking enforcement of prior Orders of this Court.

IT IS FURTHER ORDERED that Eugene Dalton and Arizona Fuels Corporation, Defendants in this action, are found to be in contempt of this Court's Orders entered September 27, 1977; November 29, 1977; April 13, 1978; and July 20, 1978; and shall be fined $1,000.00 per day each, until such time as they show compliance with the Orders of this Court, or produce evidence of their inability to comply with the Court's Orders. Said evidence shall include, at a minimum, the books and records of Defendant Arizona Fuels Corporation and the personal books and records of Eugene Dalton, and shall further include the testimony of Eugene Dalton and any other persons necessary to establish the validity of the records and books produced. Said fines shall run from a date one week (seven days) after entry of this Order.

IT IS FURTHER ORDERED that a Bench Warrant shall issue the Eugene Dalton seven days after entry of this Order. He shall remain incarcerated until such time as either (1) compliance with the prior Orders of this Court has been proved to the Court or, (2) Defendants have shown their inability to comply with the prior Orders of the Court.

IT IS FURTHER ORDERED that costs are awarded to Plaintiff.

DATED this 25th day of March, 1980.

/s/ C. A. MUECKE
C. A. Muecke
Chief Judge

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

No. CIV 77-689 PHX CAM

UNITED STATES OF AMERICA, *Plaintiff,*

v.

ARIZONA FUELS CORPORATION, and EUGENE DALTON, President, *Defendants.*

Order

(Filed June 26, 1980)

The Court, having received and considered the proposed form of Judgment submitted by plaintiffs in this matter on June 3, 1980, and having considered the defendants' objections filed June 18, 1980, finds and concludes as follows:

The payment by defendants of $450,990.54 on August 17, 1978, was for purchase of entitlements from the department's August, 1978, entitlement list as is reflected in the Court's Order of July 20, 1978.

The payment into Court of $490,441.56 on March 31, 1980, in no way reduces the interest accrued through March 25, 1980, and can only affect the interest accrued after March 31, 1980.

The fact that the Court has stayed action on civil penalties in no way affects the fact that defendants are liable for civil penalties for failure to pay the entitlement obligations that are the subject of this lawsuit and the judgment entered this date. The record is replete with evidence of defendants' willful failure to pay its entitlement obligations, and the Court finds that the proposed penalty is more than just, particularly in light of the fact that the fine could legally exceed $20,000,000.

The burden the defendants have to show that they cannot pay the judgment as entered does not extinguish the obligation, but goes to the question of whether or not they

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should be held in contempt for failure to do so together with any penalties that might be assessed should they be held in contempt.

Therefore,

IT IS ORDERED that the proposed form of judgment submitted by plaintiff shall be entered forthwith and shall be satisfied in full within 30 days of entry of this Order.

DATED this 26th day of June, 1980.

/s/ C. A. MUECKE
C. A. Muecke
Chief Judge

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

No. CIV 77-689 PHX CAM

UNITED STATES OF AMERICA, *Plaintiff,*

v.

ARIZONA FUELS CORPORATION, and EUGENE DALTON, President, *Defendants.*

Judgment

(Filed June 26, 1980)

It is hereby ORDERED AND ADJUDGED:

that plaintiff, the United States of America, recover from defendants, Arizona Fuels Corporation and Eugene Dalton, the sum of $941,432, with interest thereon in the amount of $325,459.74, plus a civil penalty in the amount of $1,000,000, and plaintiff's costs of action; and it is further ORDERED AND ADJUDGED

that the Complaint is dismissed with respect to all non-final decisions of the Department of Energy from which appeals have been taken; and it is further ORDERED AND ADJUDGED

that defendants shall fully comply on a timely basis with their entitlement obligations as they arise on a monthly basis, in accordance with 10 C.F.R. §211.67 and orders of this Court.

DATED this 26th day of June, 1980.

/s/ C. A. MUECKE
C. A. Muecke
Chief Judge

APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

No. CIV 77-689 PHX CAM

UNITED STATES OF AMERICA, *Plaintiff,*

v.

ARIZONA FUELS CORPORATION, and EUGENE DALTON,
Defendants.

Order

(Filed July 28, 1980)

The Court has received and considered defendants' motion for stay pending appeal filed July 21, 1980, pursuant to Rule 62, Federal Rules of Civil Procedure, and Rule 8(a), Federal Rules of Appellate Procedure, the memorandum filed in support of said motion, the Government's response thereto, and has heard the oral arguments of the parties with respect to said motion. The defendants seek a stay of the Court's Order and Judgment filed June 26, 1980, in this action in which the Court entered judgment against defendants in the principal amount of $941,432.00 together with interest of $325,459.74 and a civil penalty of $1,000,000.00 as a result of defendants' willful failure to pay entitlements obligations in accordance with 10 C.F.R. §211.67 and the related federal statutes and regulations.

Defendants allege that the Court had no basis in the record from which the Court could conclude that defendants had willfully failed to pay their entitlements obligations. Defendants are in error.

The record discloses that defendants have been under an obligation since prior to 1977 to demonstrate to the Department of Energy, or its predecessor, why they should not be required to pay their entitlements obligations. Defendants have repeatedly asserted that they are financially unable to pay their entitlements obligations and yet, despite

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innumerable opportunities to do so, have failed to produce a shred of credible evidence in support of their argument.

Instead, at a hearing held earlier this year the controller for Arizona Fuels, Quinn Stirland, who was hired by defendant Dalton, testified that Arizona Fuels had lent defendant Eugene Dalton $2,650,000.00, as of October 31, 1979, which was used by defendant Dalton to purchase the San Miguel Ranch; that Arizona Fuels lent San Miguel Ranch $250,000.00 to use in purchasing a $289,000.00 airplane; and that defendant Dalton had numerous cash accounts in various banks in Utah and Nevada which held funds allegedly belonging to defendant Arizona Fuels but which were in the name of Dalton, his children, his wife or his former wife. The record also reflects that Arizona Fuels invested approximately $250,000.00 in an exploration project, referred to as the Asphalt Ridge Project, at a time when it was claiming that it was unable to pay its entitlement obligations. Mineral exploration is a venture unrelated to the operation of a refinery. Defendants have made no showing, nor have they even attempted to show, that the funds lent to Dalton (or San Miguel Ranch), or used for Dalton's benefit, were ordinary and necessary business expenses for Arizona Fuels or that the manner of use of said funds — which total at least $3,000,000.00 and may exceed $8,000,000.00 — served any other necessary business purpose.

Furthermore, defendants have had the burden of making at least a reasonable showing of inability to pay for entitlements ever since the institution of agency proceedings, long before the instant action was filed. Defendants have made no serious effort to do so. In an attempt to determine defendants' ability or inability to pay, the Court took it upon itself to order the Government to institute discovery proceedings regarding the financial condition of Arizona Fuels and Eugene Dalton, even though the burden to do so is not the Government's burden. At a recent contempt hearing the Government was able to put on some of the evidence noted above and no evidence was offered, by way of offer of proof

or otherwise, to show that Arizona Fuels had a legitimate business purpose in mind when it undertook to conceal funds and bank accounts.

In addition, the Court questions the disinterestedness of defendants' attorney Leroy Axland, and his professed concern for his client's purported lack of opportunity to present evidence of his inability to pay. Mr. Axland has repeatedly asserted that his clients were and are without funds to satisfy their entitlements obligations, yet at the hearings held earlier this year it was brought out by the Government, pursuant to the discovery proceedings ordered by this Court, that one or more of Arizona Fuels' accounts was in Mr. Axland's name, and that one account had held, at one time or another (and apparently still held) several thousand dollars. Mr. Axland has not shown himself to have made any diligent effort to place evidence before this Court of his clients' inability to pay despite having had three years in which to do so.

In sum, the record in this matter, including the evidence adduced at the hearings held this year, compel the conclusion that defendants have willfully avoided paying the entitlements obligations which are the subject of this lawsuit, and the entitlements obligations which are presently accruing and which are the subject of ongoing contempt proceedings in this Court, and have willfully failed to make any effort to meet their burden to prove financial inability (to the extent of barely avoiding arrest for contempt of this Court's Order). The record reflects that neither Arizona Fuels nor its president and principle stockholder, Eugene Dalton, have made any voluntary effort in the three years in which this lawsuit has been pending to pay Arizona Fuels' entitlements obligations, and have taken every opportunity to delay the proceedings here and forestall, to the extent possible, judgment day in this case.

In accordance with the foregoing,

IT IS ORDERED that defendants' motion for stay pending appeal is denied and defendants shall satisfy the judgment

previously entered in this matter before the close of business today.

IT IS FURTHER ORDERED that should the judgment not be satisfied as prescribed above, defendant Eugene Dalton and counsel for Arizona Fuels Corporation shall appear in Courtroom 2, United States Courthouse, Phoenix, Arizona, on Tuesday, July 29, 1980, at 9:00 a.m., to show cause why defendants should not be held in contempt for failure to comply with this and prior orders of this Court.

IT IS FURTHER ORDERED that the parties shall appear in the above courtroom on Wednesday, September 24, 1980, at 9:00 a.m., for the purpose of determining whether Arizona Fuels Corporation and Eugene Dalton are financially able to meet the entitlement obligations incurred subsequent to July, 1977. Should it be proven that Arizona Fuels Corporation and/or Eugene Dalton are or were able to pay any significant amount toward entitlement obligations incurred subsequent to July, 1977, the contempt fines previously levied by this Court shall be effective as of the date they were initially levied, and will be due and payable immediately. The Court will consider reducing the fines if Arizona Fuels and Eugene Dalton meet their entitlements obligations, insofar as financially feasible, prior to the September hearing.

DATED this 28th day of July, 1980.

/s/ C. A. MUECKE
C. A. Muecke
Chief Judge

APPENDIX E

Temporary Emergency Court of Appeals of The United States

No. 9-53

UNITED STATES OF AMERICA,
PLAINTIFF-APPELLEE,

v.

ARIZONA FUELS CORPORATION, AND
EUGENE DALTON, President,
DEFENDANTS-APPELLANTS.

No. 9-54

UNITED STATES OF AMERICA,
PLAINTIFF-APPELLANT,

v.

ARIZONA FUELS CORPORATION, AND
EUGENE DALTON, President,
DEFENDANTS-APPELLEES.

Appeal from the United States District Court
for the District of Arizona

(No. CIV 77-689 PHX CAM)

(Argued: November 24, 1980 Decided: December 24, 1980)

ALAN S. NOVINS (Argued), of Lobel, Novins & Lamont, Washington, D.C., with whom Martin Lobel, of the same firm, and Leroy Axland, Sutter, Axland & Armstrong, Salt Lake City, Utah, were on the briefs for Arizona Fuels Corporation and Eugene Dalton.

KENNETH J. BARNES (Argued), of the Civil Division of the Department of Justice, Washington, D.C., with whom Dennis G. Linder and R. John Seibert, of the same Division, and Alice Daniel, Assistant Attorney General, and Michael D. Hawkins, United States Attorney, were on the briefs for the United States of America.

Before: ESTES, BECKER, and DUNIWAY, *Judges*

DUNIWAY, *Judge*:

In No. 9-53 Arizona Fuels Corporation and its sole stockholder and President, Eugene Dalton, appeal from those parts of the district court's judgment that order them to comply with the Old Oil Allocation Program, 10 C.F.R. § 211.67 (Entitlements Program), to pay $941,432 plus $325,459.74 in interest for unpaid entitlements obligations, and to pay a civil penalty of $1 million.

In No. 9-54 the United States appeals from the district court's dismissal of its claim against Dalton and Arizona Fuels for additional unmet entitlements obligations as to which exception applications are currently pending before the Federal Energy Regulatory Commission (Commission).

We affirm in No. 9-53; we reverse in No. 9-54.

I. *The Facts*

Briefly stated, "[t]he Entitlements Program, [10 C.F.R. § 211.67,] requires refiners who run a greater percentage of lower tier price controlled crude than the national average to purchase entitlements from those refiners who run a smaller percentage than the national average, thereby equalizing the cost of crude oil for all refiners." *Husky Oil Co. v. Department of Energy*, 582 F.2d 644, 645 (Em. App. 1978) (footnote omitted). For a more detailed description of the Entitlements Program, see *Pasco, Inc. v. FEA*, 525 F.2d 1391, 1395 (Em. App. 1975); *Cities Service*

Co. v. FEA, 529 F.2d 1016, 1020-1021 (Em. App. 1975), *cert. denied*, 426 U.S. 947 (1976).

On the basis of information supplied by the refiners, entitlements obligations are published by the Department of Energy (Department) each month and are payable to refiners in a sell position by the end of the month. 10 C.F.R. § 211.67(b), (c), (i). A refiner may appeal its entitlements obligation, 10 C.F.R. § 205.100 *et seq.*, as well as apply to the Office of Hearings and Appeals (OHA) of the Department for exception relief from its obligation to purchase entitlements because of "serious hardship or gross inequity." 10 C.F.R § 205.50(a)(1).

Arizona Fuels is a small, independent refiner, and until August, 1975, was a seller of entitlements because of its use of a high proportion of more expensive new oil. In that month, however, it began to use a greater proportion of old oil and thus became subject to Department orders to buy entitlements. It quickly fell into arrears, and in September, 1977, the United States brought this action. At that time, Arizona Fuels owed approximately $1 million in unpaid entitlements.

After a hearing, the district court, on September 27, 1977, issued a temporary restraining order directing Arizona Fuels and Dalton to comply with the Entitlements Program in future months. This order was extended indefinitely, after a second hearing, on November 29, 1977. Because Arizona Fuels still failed to comply with its entitlements obligations, the court, on February 9, 1978, ordered Arizona Fuels and Dalton to show cause why they should not be found in contempt.

After a contempt hearing, the court, on April 13, 1978, issued a third order requiring Arizona Fuels and Dalton to pay all entitlements obligations accruing since September 27, 1977. The court further ordered them to place in escrow any funds received from a legal action concerning Major Oil Co., a subsidiary of Arizona Fuels, for the

purchase of entitlements. The court stated that "[i]n the event that these escrow funds are not sufficient to cover the costs of purchasing entitlements . . . the burden is on the defendants to make a clear and specific showing of impossibility to comply rather than a conclusory affidavit such as that filed by Eugene Dalton. This showing should include the production of defendants' books at any future hearings on this matter to substantiate the claim, and the appearance of defendant to take the stand and testify under oath . . . ."

The court reaffirmed its April 13 order by an order of July 20, 1978, following a hearing on Arizona Fuels' and Dalton's motion for reconsideration or stay of the April order. At this hearing the parties agreed to file cross motions for summary judgment, and oral argument was held on these motions in October, 1978.

The case was dormant during 1979, but Arizona Fuels and Dalton continued to defy the Entitlements Program. Thus, in February, 1980, when the court granted an order to show cause why Arizona Fuels and Dalton should not be held in contempt, Arizona Fuels' unpaid entitlements obligations had reached the commanding figure of nearly $20 million. A show cause hearing was held March 17, 1980.

On March 25, 1980, the court issued an order finding Arizona Fuels and Dalton in contempt of court and fining each of them $1,000 a day until they complied with the orders of the court or showed evidence of their inability to comply. The court also granted the government's motion for summary judgment as to Arizona Fuels' entitlements obligations incurred in the period from August, 1975 to July, 1977. Arizona Fuels had applied to OHA for exception relief as to these obligations, but had been granted only partial relief. Because the Commission, which now hears appeals from OHA, did not yet exist, OHA's disposition as to these entitlements was final and the court found it to be supported by substantial evidence. However, because exceptions appeals were still pending before the

Commission as to Arizona Fuels' post July, 1977, entitlements obligations, the court dismissed the government's complaint as to these "non-final" entitlements obligations. The court once again reaffirmed its earlier orders that defendants comply with the Entitlements Program.

On May 6 and 7, 1980, the court held hearings on the government's motions for imposition of sanctions and for entry of judgment. Evidence was presented with regard to defendants' financial ability to comply with Arizona Fuels' entitlements obligations, as well as their compliance with prior discovery orders, and the court entered the judgment appealed from on June 26, 1980. The court awarded the government $941,432 plus $325,459.74 in interest for pre-July, 1977 "final" entitlements obligations and further levied a $1 million civil penalty against both defendants. The court dismissed the government's complaint "with respect to all non-final decisions of the Department of Energy from which appeals have been taken"—Arizona Fuels' entitlements obligations from July, 1977, to the present, amounting to approximately $24 million. Finally, the court ordered the defendants to "fully comply on a timely basis with their entitlement obligations as they arise on a monthly basis."

II. *The Government's Appeal—No. 9-54.*

The government appeals from the dismissal of its claim to entitlements obligations as to which exception proceedings are still pending.

The Entitlements Program explicitly states that "[t]he filing of an application for an exception shall not constitute grounds for non-compliance with the requirements of the regulation, ruling or generally applicable requirement from which an exception is sought unless a stay has been issued . . . ." 10 C.F.R. § 205.50(c). Similarly, 10 C.F.R. Subpart I, § 205.120(c) reiterates: "All applicable DOE orders, regulations, rulings, and generally applicable re-

quirements shall be complied with unless and until an application for a stay or temporary exception is granted."

Arizona Fuels' entitlements obligations were payable at the end of each month in which they were published by the Department in the Federal Register. 10 C.F.R. § 211.67(c) & (i). Arizona Fuels did not receive a stay or temporary exception under C.F.R. Subpart I, § 205.120 *et seq.* or 18 C.F.R. § 140(e)(4). Indeed, it does not appear from the record that such a stay was even requested. In these circumstances, Arizona Fuels was bound to comply with its entitlement obligations, and the district court erred in dismissing the government's complaint.

III. *Defendants-Appeal—No. 9-53.*

A. *The Civil Penalty.*

Under 15 U.S.C. § 754(3)(A) a civil penalty of up to $20,000 may be imposed on a company for violation of Department regulations "with respect to activities relating to the production, distribution, or refining of crude oils." Under 15 U.S.C. § 754(4) a corporate director, officer or agent "who knowingly and willfully authorizes, orders, or performs any of the acts or practices constituting in whole or in part a violation [of the entitlements regulations] . . ." will be subject to the same penalty. In 10 C.F.R. § 205.203(a)(2) the Department interprets "each violation" to refer to each day a firm fails to meet its entitlements obligations. The $1 million penalty imposed by the court for defendants' noncompliance with their entitlements obligations is thus well within the statutory limit as interpreted by the regulation even if the penalty were only levied for defendants' failure to pay their "final" pre-July, 1977, obligations.

Although it would not appear that a finding of willfulness is necessary under the statute in order to impose civil penalties on the company as opposed to its officers, the question is of little moment in this case. Defendants' ar-

gument that their failure to comply with their obligations was not willful is without merit; "[t]he record is replete with evidence of [their] willful failure to pay [their] entitlement obligations." Order of June 26, 1980, p. 2.

Despite repeated hearings and repeated opportunities since this action was filed in 1977, defendants have failed to produce evidence of their inability to comply with their obligations. Instead, the record indicates that they could easily have complied at least with the "final" entitlement obligations due for the period August 1975 to July 1977. The sum of over $2.5 million which Arizona Fuels lent to Dalton and which Dalton used to purchase a cattle ranch for himself would easily have covered Arizona Fuels' entitlements obligations for this period.

B. *The Order to Comply with the Entitlements Program.*

The district court ordered "that defendants shall fully comply on a timely basis with their entitlement obligations as they arise on a monthly basis, in accordance with 10 C.F.R. § 211.67 and orders of this Court." Defendants mistakenly understand this order to require them to pay all of their entitlements obligations including those for which exception proceedings are yet pending. Even understood in this way, however, the order is entirely appropriate. Until a stay is *granted* or until Arizona Fuels overturns its entitlements obligations through a *successful* appeal or through the *grant* of exception relief, it is required under the regulations to pay its entitlements obligations as published by the Department in the Federal Register. It must pay these obligations whether they are past due or are just now arising. Moreover, defendants' argument that an evidentiary hearing should have been held before the issuance of this order ill suits them in light of their consistent failure to present substantial evidence of impossibility of compliance, despite numerous opportunities.

C. Order to Pay Pre-July, 1977, Entitlements Obligations.

The district court found that OHA's denial of the exception relief sought by Arizona Fuels for its pre-July, 1977, entitlements obligations was supported by substantial evidence. Defendants argue that our decision in *Husky Oil Co. v. DOE*, 582 F.2d 644 (Em. App. 1978) requires that we reverse this portion of the district court's judgment.

In *Husky* we held that the Department's explicit use of a negative profit margin "for purposes of evaluating current financial posture and determining exception relief" was invalid. 582 F.2d at 653. But here there is nothing in the record to indicate that OHA knew or should have known that its action on Arizona Fuels' applications for exception relief would impose a negative profit margin on the company. And in any event, defendants did not present substantial evidence before the district court showing that payment of these obligations would have forced the company to operate at a loss. Indeed, the record shows that the company could easily have paid these obligations.

"In the absence of exceptional circumstances not present in these cases, there is a rebuttable presumption of validity of findings of fact by [the] administrative agency, which casts the burden of proof of invalidity on the party challenging the findings of fact. *Anniston Manufacturing Co. v. Davis*, 301 U.S. 337, 357, 57 S.Ct. 816, 825, 81 L.Ed. 1143, 1156 (1937); *Coleman v. PACCAR, Inc.*, 424 U.S. 1301, 1306, 96 S.Ct. 845, 848, 47 L.Ed.2d 67, 72 (1976) . . ." *Petraco Valley Oil & Refining Co. v. DOE*, ___ F.2d ___ (TECA Nos. 5-47 and 5-48, 1980).

Arizona Fuels and Dalton have not met their burden of proof. The cause of Arizona Fuels' financial condition is not the entitlements program, from which defendants profited, but is defendant Dalton's draining away from Arizona Fuels of its financial resources.

D. *Dalton's Liability.*

Finally, Dalton argues that he should not be held personally liable for Arizona Fuels' unmet obligations.

Dalton is President and sole stockholder of the company. The record shows that large amounts of corporate funds have been diverted to Dalton's personal use. ". . . [W]here the corporation['s] . . . financial resources are drained off by the controlling shareholder . . ., there is more justification for holding the latter liable . . . ." Henn, *Corporations*, 2d ed. (West), 252, 254. See also cases noted in 51 Harv. L. Rev. 1401, 1402, and 14 Cal. L. Rev. 19–21. Dalton cannot feign ignorance of the company's entitlements obligations. In these circumstances, the district court was correct in holding Dalton jointly liable for Arizona Fuels' entitlements obligations.

In No. 9–53 the judgment is affirmed. In No. 9–54 the portion of the judgment appealed from is reversed and the matter is remanded for further proceedings consistent with this opinion.

APPENDIX F

TEMPORARY EMERGENCY COURT OF APPEALS
OF THE UNITED STATES

No. 9-53 & 9-54

UNITED STATES OF AMERICA, *Plaintiff-Appellee,*

v.

ARIZONA FUELS CORPORATION, and EUGENE DALTON, President, *Defendants-Appellants*

Before ESTES, BECKER, and DUNIWAY, *Judges.*

Upon consideration of Appellants' Petition for Rehearing,

IT IS HEREBY ORDERED that said Petition is DENIED. The mandate will issue February 9, 1981.

FOR THE COURT:

/s/ MICHAEL S. LEVINE
Michael S. Levine
Deputy Clerk

February 2, 1981

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